CASEY, GENTZ & MAGNESS, L.L.P.
ATTORNEYS AT LAW

98 San Jacinto Blvd., Ste. 1400
Austin, Texas 78701-4286
Phone 512-480-9900
Fax 512-480-9200
www.phonelaw.com

Robin A. Casey
Susan C. Gentz
Diane M. Barlow
Valerie P. Kirk
Bill Magness
Bradford W. Bayliff

July 18, 2007

The Honorable Deborah Taylor Tate
Federal Chair, Federal-State Joint Board on Universal Service
Federal Communications Commission
445 12th Street, SW, Portals II, Room 8-A204
Washington, DC 20554

Commissioner Ray Baum
State Chair, Federal-State Joint Board on Universal Service
Oregon Public Utilities Commission
550 Capitol Street, SE, Suite 215
Salem, OR 97308

Re: *High-Cost Universal Service Support, WC 05-337*
Federal-State Joint Board on Universal Service, CC Docket 96-45

Dear Commissioner Tate and Commissioner Baum:

On July 12, 2007, an Ex Parte was filed by Century Tel, Inc., Consolidated Communications, Inc., Embarq Corporation, and Windstream Communications, Inc. presenting a study (the "Four-Company Study"), purportedly analyzing the profitability of providing supported services in certain wire centers in Texas.[1] Although the companies portray the Four-Company Study as providing answers and insights useful to the Joint Board, the Texas USF Reform Coalition's[2] preliminary evaluation concludes that the analysis raises far more questions than it answers, and should be disregarded by the Joint Board until it can be reviewed in the upcoming contested case in Texas.

1 *See* "Universal Service Funding: Realities of Serving Telecom Customers in High Cost Regions," Balhoff & Rowe LLC, Summer 2007, attached to Ex Parte Filing of Century Tel, Inc., Consolidated Communications, Inc., Embarq Corporation, and Windstream Communications, WC 05-337 and CC Docket 96-45, July 12, 2007.

2 The Texas USF Reform Coalition is comprised of the Texas Cable & Telecommunications Association, Time Warner Telecom of Texas, L.P. and Sprint Nextel.

We note that the Four-Company Study is based entirely on confidential information provided by these companies to their consultant, including one or more "company-generated" cost models "similar to the HAI model" that have never been disclosed, and are described in the vaguest of terms in their filing.[3] Importantly, the study never produces the "company-generated forward-looking models" upon which it relies, nor does it explain how and when the study is adjusted for other inputs supplied by the companies. There are no comparisons made between the models that describe their similarities or differences. Nor does the "study" disclose the methodology used to exclude the revenues and costs of non-supported services, which is particularly important given that most related services rely on the same local loop as supported services and the allocation (or lack thereof) of loop costs (and/or the inclusion of other service-revenues) plays a large role on the financial viability of all local network investments. The Four-Company Study also fails to consider any alternative technologies that might serve rural areas more efficiently. Nor does it examine or explain why incumbents should be subsidized in areas that competitive carriers serve without receiving subsidies. The Four-Company Study is the ultimate "black box," full of asserted results, but with virtually no supporting analysis. Ultimately, it is simply a lengthy re-statement of the obvious; it is more expensive (all things, other than population density, being equal) to serve customers in rural areas than those residing in towns.

The only unambiguous fact that can be gleaned from the study is that the study's results are completely unrelated to reality. Specifically, the study *models* a cost structure that produces an average return on investment ("ROI") for these companies of only 7%, going so far as to claim that additional USF subsidy may be needed to bring their earnings closer to a target 10%.[4] The Earnings Monitoring Reports filed with the Texas Public Utility Commission by the same companies supporting the study, however, demonstrate that USF subsidies are today supplying *excessive* returns, with the average ROI of the modeled companies of 40%, *more than 5.5 times* the return estimated by the company-generated models, and *four times more* than the ROI identified as reasonable by the Study (10%).

---

3 For instance, the description of the basic methodology used in the Four-Company Study:

> The modeled cost and investment data used in this report are also forward-looking, with some of the inputs updated by the companies to reflect underlying and verifiable current costs.... The model also proposes operating costs, which are particularly helpful in this study since it is difficult and contentious to allocate overhead and other supra-wire-center operations to an individual switching center.
>
> ***
>
> This [Four-Company] study focuses on "supported services" – those for which USF monies are paid – excluding other services which may or may not be included in the carrier's products sold to retail and wholesale customers. Some revenues and costs associated with non-supported services are eliminated from this study ...

Four-Company Study, footnotes 8 and 9 respectively.

4 Four-Company Study at 23, concluding that the "...study indicates a potential need for additional support given that the 7% ROI for all wire centers including USF receipts remains below the assumed cost of capital hurdle [10%]."

Comparing ROI Estimated by Company-Generated Cost Models to Actual ROI Reported by Company to Texas PUC[5]

Four Companies	Actual ROI	Actual ROE
Consolidated	23%	48%
Windstream	128%	379%
Century	21%	21%
Embarq	Data Claimed Confidential	
Average	40%	97%
ROI Estimated by Models	7%	

The Texas USF Reform Coalition is not suggesting that the Joint Board should attempt to reconcile the claims made in the Four-Company Study with the returns actually enjoyed by its sponsors. There is simply no need for that debate to occur before your group. Fortunately, the Public Utility Commission of Texas is planning to soon initiate a contested case to address these issues. In that forum, the critical tools of discovery and cross-examination will be available to look beyond the curtain of confidentiality that masks the methodology used in the Four-Company Study. The Texas Commission's thorough examination of the facts will likely explain why the Four-Company Study generates results that are so at odds with publicly available data the sponsoring companies have filed to date. We recommend that the Four-Company Study be set aside until the completion of the Texas Commission's contested case, and that the Joint Board not rely on the analysis in reaching its own findings or conclusions.

Respectfully submitted,

CASEY, GENTZ & MAGESS, L.L.P.

Bill Magness

Robin A. Casey
Bill Magness

COUNSEL FOR THE TEXAS USF REFORM COALITION

cc: Chairman Paul Hudson, PUCT
Commissioner Julie Parsley, PUCT
Commissioner Barry Smitherman, PUCT

---

[5] 2005 Annual Earnings Monitoring Reports Filed in Public Utility Commission of Texas Project 32533.